

Internal Revenue Service

Department of the Treasury

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Washington, DC 20224

Date 9/29/95
Bureau [redacted]

Person to Contact: [redacted]

Telephone Number: [redacted]

Refer Reply to: [redacted]

Date: AUG 14 1995

E.I.N: [redacted]
Key District: Baltimore

Dear Applicant:

We have considered your application for recognition of exemption under section 501(c)(3) of the Internal Revenue Code. Based upon the information submitted we conclude that you do not qualify for exemption under that section. The basis for our conclusion is set forth below.

The information submitted indicates that you were incorporated on [redacted] under the laws of the State of [redacted]. Your articles of incorporation provide that you are organized "to promote the Christian philosophy of life and Christian values through the creation and dissemination of Christian-oriented materials to individuals and organizations in the United States and worldwide."

You indicate that you will be involved in the production and dissemination of Christian-oriented and educational materials, including, but not limited to: (i) operation of a resource center which will sell Christian and educational recordings including sermons and musical recordings to the general public; (ii) production and dissemination of catalogs and other promotional materials relating to the resource center; (iii) creation and production of programs and program segments for broadcast on religious radio programs and television programs; and (iv) production and dissemination of printed material in support of Christian-oriented and educational operations.

The financial data provided by you indicates that in fiscal years [redacted], [redacted] and [redacted] you anticipated receiving approximately [redacted]% of your income from unrelated business income and about [redacted]% of your income from gifts, grants and contributions.

Organizations described in section 501(c)(3) of the Code are exempt from federal income taxation under section 501(a). To be included within section 501(c)(3), an organization must be "organized and operated exclusively for...religious, charitable,... literary, or educational purposes,...no part of the net earnings of which inures to the benefit of any private shareholder or individual."

Section 1.501(c)(3)-1(a) of the Income Tax Regulations

states that in order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt. An organization is organized exclusively for one or more exempt purposes only if its articles of organization limit the purposes of such organization to one or more exempt purposes and do not expressly empower the organization to engage, otherwise than as an insubstantial part of its activities, in activities which in themselves are not in furtherance of one or more exempt purposes.

Section 1.501(c)(3)-1(b)(1)(iii) of the regulations states that an organization is not organized exclusively for one or more exempt purposes if its articles expressly empower it to carry on, otherwise than as an insubstantial part of its activities, activities which are not in furtherance of one or more exempt purposes.

Pursuant to section 1.501(c)(3)-1(b)(4) of the regulations, an organization is not organized exclusively for one or more exempt purposes unless its assets are dedicated to an exempt purpose. An organization's assets will be considered dedicated to an exempt purpose, for example, if, upon dissolution, such assets would, by reason of a provision in the organization's articles or by operation of law, be distributed for one or more exempt purposes, or to the Federal Government, or to a State or local government, for a public purpose, or would be distributed by a court to another organization to be used in such manner as in the judgment of the court will best accomplish the general purposes for which the dissolved organization was organized.

Article Three of your articles of incorporation states that you are organized for the purpose of promoting the Christian philosophy of life and Christian values through the creation and dissemination of Christian-oriented materials. This purpose without more, as stated in your articles of incorporation, meets the requirements of section 1.501(c)(3)-1(b)(iii) of the regulations. However, contrary to the requirements of section 1.501(c)(3)-1(b)(4) of the regulations, your articles are silent as to the distribution of your assets in the event of your dissolution and your articles do not provide that your assets are dedicated exclusively to an exempt purpose.

Section 1.501(c)(3)-1(c) of the regulations provides the second test each organization must meet in order to qualify as an organization exempt under section 501(c)(3) of the Code. Under such section, an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its

activities is not in furtherance of an exempt purpose.

The exempt purposes listed in section 501(c)(3) of the Code and section 1.501(c)(3)-1(d)(1) of the regulations include: religious, charitable, scientific, testing for public safety, literary, educational or prevention of cruelty to children or animals. An organization may be exempt as an organization described in section 501(c)(3) if it is organized and operated exclusively for one or more of such purposes.

Section 1.501(c)(3)-1(d)(2) of the regulations provides that the term "charitable" as used in section 501(c)(3) include the "advancement of religion."

To meet the requirement for the operational test, "the purpose towards which an organization's activities are directed, and not the nature of the activities themselves, is ultimately dispositive of the organization's right to be classified as a section 501(c)(3) organization." Presbyterian & Reformed Publishing Co. v. C.I.R., 79 T.C. 1070, 1082 (1982), quoting B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352, 356-357 (1978). Whether an organization satisfies the operational test is a question of fact. See, B.S.W. Group, Inc. v. Commissioner, supra. Because exemption will be granted only if the organization is organized and operated "exclusively" for exempt purposes, the presence of a single nonexempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes. See, section 1.501(c)(3)-1(c)(1) of the regulations. If no substantial nonexempt purpose exists, the income from trade or business may be exempt if the activity is carried on in furtherance of an exempt purpose. Accordingly, prior to granting you an exempt status under section 501(c)(3), we must determine toward what end are your activities directed and whether such activities have their basis in a substantial commercial purpose.

To assist themselves in deciding whether the activities of an organization are conducted for an exempt purpose, the courts have generally focused on how an organization carries on its activities, implicitly reasoning that an end can be inferred from the chosen means. Although no one factor is determinative, the courts have looked at various factors in making their decisions.

One of the first cases where exemption was denied to a religious publishing house is Scripture Press Foundation v. United States, 285 F.2d 800 (1961), cert. den., 368 U.S. 985 (1962). There the organization was devoted to publishing religious materials for Sunday school instruction. The court in Scripture Press Foundation found that factors such as the particular manner in which an organization's activities are conducted, the commercial hue of those activities, and the existence and amount of annual or accumulated profits are

relevant evidence of an impermissible predominant purpose.

You have stated that your activities will consist of production and dissemination of Christian-oriented educational recordings, including sermons and musical recordings; operation of the resource center disseminating such materials; and production and dissemination of catalogs and other promotional material related to the resource center. You have provided us with copies of your promotional materials and copy of a catalog. The catalog, similar to those used by a for-profit commercial business, provides pictures and description of the audio cassettes and compact discs for sale and the price of each item. Your catalog also contains advertisements for two organizations, a travel company and a printing company. After reviewing your promotional materials and catalog, we do not believe that your services and activities are conducted in a manner different from any other commercial business selling musical recordings and printed literature. The manner in which an organization conducts its activities is strong evidence of the predominance of nonexempt commercial purposes. See, United Missionary Aviation, Inc., TC Memo 1990-566, and Scripture Press Foundation, *supra*.

Competition with commercial firms also is strong evidence of a substantial nonexempt purpose. See, B.S.W. Group, Inc., *supra*. Commercial firms which sell secular musical recordings generally also sell religious recordings. The sale of audio cassettes and compact discs in the manner described by you is in competition with such for-profit businesses. Because your promotional materials or your catalog do not state otherwise, we assume that the musical recordings and religious literature sold by you is available in the market from other sources. Since the conduct of this business is your primary activity, we believe that such facts weigh heavily against exemption.

Whether an organization provides its materials at or below cost is another consideration in determining whether such organization has a commercial purpose. United Missionary Aviation, Inc., *supra*. The prices stated in your catalog for the audio cassettes and compact discs seem comparable to audio cassettes and compact discs sold by commercial firms. You have not indicated to us, and you do not advertise to your potential customers, that the musical recordings are sold at or below cost.

Substantial profits, while not determinative, also indicate that an organization's primary purpose is commercial in nature. Scripture Press Foundation, *supra*. In the financial data submitted with your application, you do not anticipate any excess revenues over expenses for the fiscal years [REDACTED], [REDACTED] and [REDACTED]. However, under line 22 of the financial data you show expenses of \$[REDACTED], \$[REDACTED] and \$[REDACTED] in fiscal years [REDACTED], [REDACTED] and [REDACTED], respectively, under the category "other." You have not attached, as required by the Service, a schedule of such

[REDACTED]

expenditures. Assuming that these are not salaries and wages (since there is a separate line item for these expenses), we believe that such amounts, or at least a portion thereof, are profits. In addition, the [REDACTED], a newsletter submitted by you, indicates that you anticipate earning a profit from sale of the broadcast tapes and sharing the profit with [REDACTED] telecast and [REDACTED] radio broadcast.

Lastly, you have stated in your application that approximately [REDACTED] % of your income will be unrelated business income. This fact also indicates that a substantial amount of your activities will have a commercial hue.

Therefore, based upon the factors discussed above, we have concluded that your activities have their basis in a substantial nonexempt purpose, furthering a commercial endeavor. Your religious purposes are incidental to your commercial endeavor of selling religious literature.

As discussed previously, your articles of incorporation do not provide that should you dissolve, all of your assets will be distributed to another charitable entity or a governmental body. Therefore, it is possible for your earnings to be distributed to private persons or to further non-exempt ends. This suggests that private inurement or benefit is possible, which is specifically prohibited under section 501(c)(3).

We have previously ruled that a non-profit organization operated in a non-commercial manner and formed to educate the public through dissemination of printed materials and radio broadcasts may qualify for exemption from federal income tax under section 501(c)(3) on the basis of being an educational organization. See, Rev. Rul. 67-342, 1967-2 C.B. 187; Rev. Rul. 68-563, 1968-2 C.B. 212 and Rev. Rul 76-4, 1976-1 C.B. 145, compare, Rev. Rul. 60-351, 1960-2 C.B. 169 and Rev. Rul. 77-4, 1977-1 C.B. 141. Because you are operated in a commercial manner, this reason in and of itself causes you not to qualify as an educational organization under section 501(c)(3).

Based upon the above discussion, we conclude that you do not qualify for exemption under section 501(c)(3) of the Code. You are required to file federal income tax returns on Form 1120.

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that

[REDACTED]

person will need to file a proper power of attorney and otherwise qualify under our Conference and Practices Requirements.

If you do not protest this ruling in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgement or decree under this section shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within 30 days, this ruling will become final and copies will be forwarded to your key district office. Thereafter, any questions about your federal income tax status should be addressed to that office.

You will expedite our receipt of your reply by using the following address on the envelope:

Internal Revenue Service
[REDACTED]
1111 Constitution Ave, N.W.
Washington, D.C. 20224

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

(Signed) [REDACTED]

[REDACTED]
Chief, Exempt Organizations
Technical Branch 4

[REDACTED]

8-11-95

[REDACTED]

8-14-95